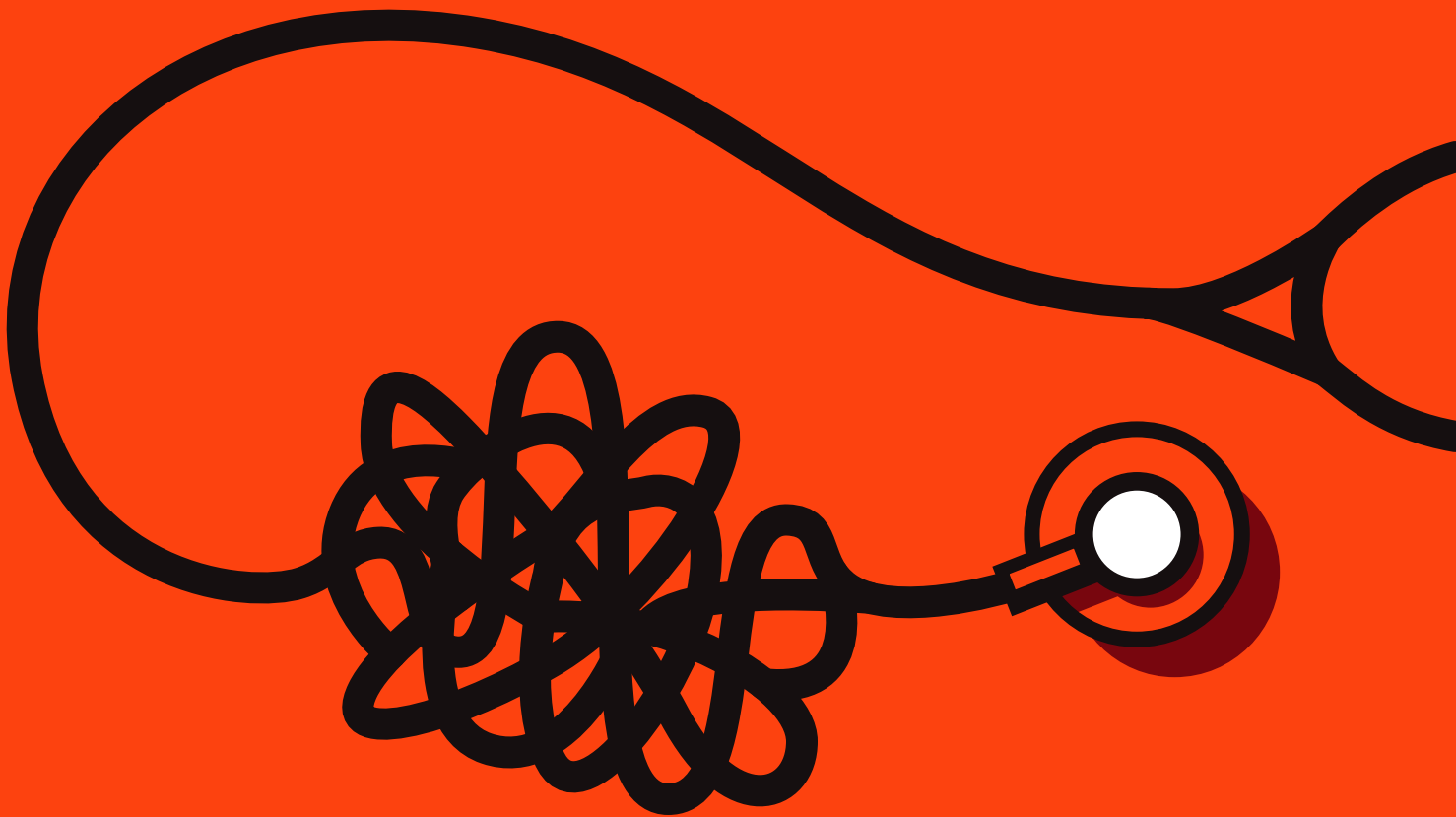


FEE's Guide to Health Care

ANSWERS TO THE
**HEALTH CARE
CONUNDRUM**



FEE's Essential Guide to Health Care Reform

*Essays from the Foundation
for Economic Education*

FEE

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Introduction

Health care policy rocks elections and dominates headlines for reason. It gets to the core of how we live, even whether we live. The issue comes down to this. Should we trust government to manage this? Or should we let the competitive forces of the market deliver what we need?

You can gain some insight by reflecting on other parts of your life. Where do you shop for groceries, clothing, computers, make up? Do we have national plans and bureaucracies managing their creation and delivery? Absolutely not. We've learned from experience that leaving these sectors to market forces reduces prices, incentivizes creativity, and leads to mass consumption.

This is precisely how health care became amazing in the modern era. Government had no involvement at all until the first decade of the 20th century. Even then, it was mostly limited until after World War II. But the greatest explosion of health ever recorded in human history occurred in the 2nd half of the 19th century, before government had any hand in health care.

It is clear where we need to be headed with policy. But that is easier said than done. There are special interests. There are payoffs. There are bureaucracies to feed and politicians who wanted to demagogue the issue to achieve reelection. Unraveling this mess is a serious challenge. The main challenge is intellectual: all of us need to understand. This is the first step.

What follows is the essential guide to that understanding.

This Is Why Government Shouldn't Be Involved in Healthcare

Jeffrey Tucker

The Republican-controlled House vote to “repeal Obamacare” – if that is what this was – was a stunning mess.

Did they get it right? The answer is obviously no, and that’s inevitable. Just imagine a bill that sets out to reorganize any industry that is currently mostly market driven, such as shirts, software, groceries, or furniture. Would any bill coming from Congress that pertains to the whole of any of these be wonderful? It’s impossible.

This is because the minds of politicians working together – with all their mixed motives of special-interest acquiescence, electoral fears, and general ignorance – cannot possibly replicate, much less improve upon, the brilliant mind of the market at work.

Fortunately, we don’t have to deal with such bills in most markets. But the healthcare industry is different. It’s been heavily regulated for more than a century. Obamacare went in the wrong direction, toward more rather than less government control. It actually disabled the mind of the market. The result has been soaring deductibles and premiums, insurers going belly up, and average citizens being forced to pay for insurance they can’t afford to use.

Change is necessary. Sadly, any structural change in the industry is pushed through via legislation. That is a tragedy. The challenge is to sort

out real vs. **fake reform**, and do this amidst grandstanding, bombast, posturing, ideological panic, rhetorical bombast, and media mania.

The Miasma of Politics

The House had little more than one day to consider a bill that would affect the lives of every single living American in the most fundamental way. Meanwhile, those of us in the peanut gallery had to try to make sense of whether or not this bill is a promising development, remembering that not backing something necessarily means de facto settling with the legislative status quo.

Even getting the core facts of the legislation was a challenge.

What is the core standard by which any health care bill should be evaluated, given that nothing coming out of Congress that can gain a majority of Republicans will ever be right? The test is this: does this bill take us in the direction of restoring market competition and market signaling, or does it preserve the current managed, artificial, coercive, and unworkable system that relies on government control?

Features of Obamacare (**explains** David Henderson) disable market competition: guaranteed issue and community rating. Guaranteed issue mandates that everyone who shows up must be accepted. Community rating forbids insurance pricing from being influenced by risk assessment, which takes the insurance out of insurance. And a third issue is the one that is perhaps most absurd: essential benefits. This mandates what is covered under all health insurance, thus ruling out flexibility and choice on the part of either buyers or sellers.

A reform worthy of support must deal directly with these problems. Donald Trump does not understand this at all. He keeps tweeting that he absolutely insists on keeping the mandate that all health insurance must cover pre-existing conditions, without an awareness of what this implies about existing law. The dogmatic demand painted the Republicans in a corner. They couldn't repeal the very mandates and disabled-pricing schemes that have created such a mess in the industry.

Yet Obamacare is so bad that **some states** have toyed with actually nullifying the law. Taking their cue from such movements, the House bill encourages states to take some steps to do just that. Whether they come through or not is another matter.

Still, this amendment brought some skeptics on board. The final bill permitted the states to opt out of essential benefits and community rating mandates, thus removing Congressional culpability but allowing a decisive number of votes to come out in favor of the bill. (Whether states will actually use the waivers is **another matter**.)

Why they Will Preserve Obamacare

It's now clear where this "repeal and replace" thing is headed. A small cadre of the GOP House leadership hammered out a few tweaks of Obamacare in secret. All the essentials of Obamacare were left in place: the mandates, the regulations, the strictures, the entitlement expansions, the preset packages, and many taxes.

The glorious reform had "lame" written all over it. A mandate with penalties paid to government is replaced with a mandate to pay insurance companies plus a refundable tax credit which might actually cost more in the future than the present system.

You might say, as Reason **observed**, that it is "better than nothing." True, and Khrushchev's economic ideas were an improvement on Stalin's. Still, it's another central plan, providing no real substantial room for new innovation, competition, or genuine market forces.

When the bill was released on March 7, Trump **tweeted**: "Our wonderful new Healthcare Bill is now out for review and negotiation."

This tweet shattered the illusion that something dramatically pro-freedom would actually happen. Despite GOP control of the House, Senate, Executive Branch, and even a free-market minded head of the

Health and Human Services, the proposed reform is something that these very same people would have decried as socialism eight years ago.

Revolt Against the Regime

A few smart, principled people in the party quickly objected, with Rand Paul in the Senate and Justin Amash in the House leading the charge. They know that this is a once-in-a-lifetime opportunity to fix a healthcare system that has been getting structurally less functional for many decades, burdened down ever more with a thicket of control, subsidies, pressure-group payouts, and bureaucratic layers of rules.

They were there as Obamacare became the final disgrace of the welfare state, so bad that the former president himself didn't even mention it, much less brag about it, in his farewell address. The election was an opportunity, finally.

During the election's final weeks, Trump opposed everything about Obamacare and brought out his rhetorical blowtorch against it in the final weeks, just as premiums rose astronomically. Clinton, in contrast, promised only tweaks to make the existing system work better.

Voters revolted, hoping for some relief. Exit polls from the 2016 presidential election **told the story**. Trump had temporarily dropped even his obsessions with nationalism, protectionism, and strongman symbolism for just a few days to say something sensible: repeal and replace this monstrosity. The outrage against the prevailing system launched him into the presidency.

Now it is mid-March and the great moment has arrived. As it turns out, nearly everything is left just as it was. It's not as if Trump is doing his best to support the best-possible option. There are plenty of good plans out there. He has just rejected them in favor of the most watered-down reform possible.

Indeed, he has used the **full weight of the presidency**, all the power of his influence, and every bit of political clout he has to support the worst-available plan for dealing with the utter and complete failure of the status quo. He went so far as to invite his free-market critics to the

White House and the Oval office, gave them a chance to speak, and then finally laid out his conditions for negotiations: stop criticizing the thing he supports as merely Obamacare-Lite.

Sensing that he had a problem, Trump then **tweeted** that this was only the first stage of three, and the good stuff will come later.

Now the Congressional critics have a problem. The more they criticize the proposed reform, the less influence they will have over the process going forward. Or they can take a gamble that Trump might ultimately improve the bill under their influence, but they have to muzzle their criticisms themselves in order to be in the game at all.

And here we have the “art of the deal” in action. It is about getting something, anything, shoved through, with the right people given what they need to take credit or cast blame, depending on their appointed role in the political drama. The deal is what matters, not the actual results. I’m the last person to be a pessimist, but it looks to me like the end result will be: the codification of Obamacare in principle and practice.

It could have been otherwise, and so easily. Just imagine the power of the Trump presidency, in its earliest weeks, pushing for a real free-market solution. It might have worked. At least it would have defined the right terms: freedom vs. control. Now that theme is lost and so is the chance for real reform.

Why Am I Shocked?

On a personal note, the course of events has hit me like a sucker punch. My friends keep telling me that I was ridiculous to expect anything else. “Did you really expect something good to come of this presidency? That’s so naive. You, more than anyone, predicted that there would be no net increases in liberty from this.”

The truth is that my brain can’t work without having some hope. There had to be some good that would come from the election outcome, and surely doing something about the healthcare problem is it.

After all, even the worst US presidents have often done at least one good thing. Clinton reformed welfare. Reagan cut tax rates. Carter

deregulated. Nixon opened diplomatic relations with China. Even FDR deserves kudos: his first act as president was to repeal liquor prohibition.

So, I had it worked out in my mind that the full repeal of Obamacare and its replacement by a market-based system would be the one great thing that would happen in the Trump years. We might still get trade wars, a dangerous military build up, police-state controls on association, and travel restrictions, but at least something as important as healthcare would be brought into the 21st century.

Up with Freedom

The root problem is that the health care system is not free from government control. It's why the far-less-regulated sectors of veterinary medicine and cosmetic surgery are just fine, with declining prices, better technology, and more access. There is nothing special about medicine relative to the economic forces that manage every other good and service.

Meanwhile, my Google Home robot can bring any product to me with a voice. I can summon a burrito to my desk with a click on my watch. I can get a personal trainer to show up to my place on schedule. Everyone is competing to bring me cool stuff, often for free. With markets, everything works for you and me. Healthcare is not only failing to improve but getting more expensive, less accessible, more stuck in a bureaucratic mire.

Rand Paul offers one salient example: how about new models for price negotiation with large insurers? If regulations allowed it, people could join co-ops of any size that would work like insurance mutual funds, and managers could shop around for the best policies at the best prices. This is only one example but in order to see it, we need massive deregulation.

It is not entirely crazy that a passionate Rand Paul and his colleagues will finally prevail and get a better bill. Their commitment is obvious, and it is not just about political posturing. There are millions of human

lives at stake. We are, after all, talking about health, which is at the core of the quality of life itself. Only freedom can be trusted to manage it.

However, keep this in mind: should something good finally emerge, whether this year or next, it will be due not to the “greatness” of the executive and all his bluster, but rather to the courage, character, and commitment of a handful of people who still believe that freedom is that best path. It is not the political system that will have worked; it is that moral passion triumphed over politics.

And here we have the best possible precondition for liberating the medical sector from government: a deep and broad cultural commitment to human freedom in every area of life. Politics is not the agent of change but rather the thing that is changed. There is always hope, rarely in the political process but always in the human heart and mind.

Could the Uber Model Work?

Charles Hughes

Patients are often insulated from the cost of health care services and at an informational disadvantage. It is hard for patients to determine the quality of those services, and they do not have much of an incentive to check. This can create a situation where patients spend more for the health care services they consume, in what is called a moral hazard problem.

The Moral Hazard Problem

Moral hazard has been studied extensively from the consumer side. How providers respond in these situations is less understood, but also important. It could help explain why prices are growing rapidly in areas as diverse as health care, financial services, or even taxi rides.

If taxi drivers think their passengers lack the ability to check, they might overcharge or take a route that is longer than necessary. Riders on a business trip who are getting reimbursed by their companies might not care as much about cost, increasing the opportunity for drivers to charge more.

A new [paper](#) in the February issue of *The Economic Journal* details the extent that traditional taxi drivers charged riders more when this opportunity arose. Drivers were told the riders were new to the city and being reimbursed by employers, so there was a reduced check on the routes they took or prices they charged. Taxi drivers systematically charged these riders more.

In their experiment, the authors used a controlled field experiment to try to determine if taxi drivers charged more to riders when the rider told them their employer is reimbursing them for the trip. In this

instance, the drivers might take a longer route or overcharge because they infer that the rider does not care as much about the price, because they are not paying for it directly.

As a test, research assistants took 400 taxi rides in Athens, Greece. Each time the rider told the driver they were unfamiliar with the city. Some riders also told the drivers they needed a receipt so the expense could be reimbursed by the employer. The authors deem this the “moral hazard treatment” as the driver could now infer that the rider is less likely to notice, or report, dishonest behavior.

There are two main ways drivers could take advantage of the uninformed and insulated consumer. They could overtreat, in this case taking an unnecessarily long route or detour. They could also overcharge.

A third mechanism, undertreatment, is not as feasible for taxis rides, because even uninformed riders would likely be able to perceive if they did not arrive at their destination. In other fields, such as health care, undertreatment could be more prevalent.

Overcharged

In the experiment, riders that gave notice of employer reimbursement were 17 percent more likely to pay higher-than-justified prices for a given ride, and paid about 7 percent more on average. While there were significant differences in terms of overcharging, there was no such difference when it came to overtreatment.

This could be because drivers view overtreatment as easier to detect, as someone can tell if they are going in circles or winding their way around the city more easily than if they were simply being charged more. The extent of overcharging indicates a substantial provider response to the moral hazard problems.

In other fields where it is even harder for consumers to verify quality of services, such as finance, overtreatment and undertreatment could play a larger role.

From Taxis to Health Care

Just as with the taxi drivers in Greece, providers respond to this moral hazard problem by overcharging. The authors describe physicians in Germany, who charging patients for services that were never rendered.

One analysis by [Walmart](#) of employee experiences found that about 30 percent of the spinal procedures that employees were told they needed were not appropriate. This response from providers results in higher costs and services that consumers do not necessarily need or want.

Uber's pricing system, which requires a receipt with the name of the driver and with a map for the rider, is just one example of a new technology that protects uninformed consumers from being overcharged. Similar transparency in other fields, such as health care, could bring substantial benefits to consumers and rein in cost growth.

Real Health Insurance Is a Crime

Warren Gibson

Health insurance is a crime. No, I'm not using a metaphor. I'm not saying it's a mess, though it certainly is that. I'm saying it's illegal to offer real health insurance in America. To see why, we need to understand what real insurance is and differentiate that from what we currently have.

Real Insurance

Life is risky. When we pool our risks with others through insurance policies, we reduce the financial impact of unforeseen accidents or illness or premature death in return for a premium we willingly pay. I don't regret the money I've spent on auto insurance during my first 55 years of driving, even though I've yet to file a claim.

Insurance originated among affinity groups such as churches or labor unions, but now most insurance is provided by large firms with economies of scale, some organized for profit and some not. Through trial and error, these companies have learned to reduce the problems of adverse selection and moral hazard to manageable levels.

A key word above is unforeseen.

If some circumstance is known, it's not a risk and therefore cannot be the subject of genuine risk-pooling insurance. That's why, prior to Obamacare, some insurance companies insisted that applicants share information about their physical condition. Those with preexisting conditions were turned down, invited to high-risk pools, or offered policies with higher premiums and higher deductibles.

Insurers are now forbidden to reject applicants due to preexisting conditions or to charge them higher rates.

They are also forbidden from charging different rates due to different health conditions — and from offering plans that exclude certain coverage items, many of which are not “unforeseen.”

In other words, it’s illegal to offer real health insurance.

Word Games

Is all this just semantics? Not at all. What currently passes for health insurance in America is really just prepaid health care — on a kind of all-you-can-consume buffet card. The system is a series of cost-shifting schemes stitched together by various special interests. There is no price transparency. The resulting overconsumption makes premiums skyrocket, and health resources get misallocated relative to genuine wants and needs.

Lessons

Some lessons here are that genuine health insurance would offer enormous cost savings to ordinary people — and genuine benefits to policyholders. These plans would encourage thrift and consumer wisdom in health care planning, while discouraging the overconsumption that makes prepaid health care unaffordable.

At this point, critics will object that private health insurance is a market failure because the refusal of unregulated private companies to insure preexisting conditions is a serious problem that can only be remedied by government coercion. The trouble with such claims is that no one knows what a real health insurance market would generate, particularly as the pre-Obamacare regime wasn’t anything close to being free.

What might a real, free-market health plan look like?

- People would be able to buy less expensive plans from anywhere, particularly across state lines.

- People would be able to buy catastrophic plans (real insurance) and set aside much more in tax-deferred medical savings accounts to use on out-of-pocket care.
- People would very likely be able to buy noncancelable, portable policies to cover all unforeseen illnesses over the policyholder's lifetime.
- People would be able to leave costly coverage items off their policies — such as chiropractic or mental health — so that they could enjoy more affordable premiums.
- People would not be encouraged by the tax code to get insurance through their employer.

What about babies born with serious conditions? Parents could buy policies to cover such problems prior to conception. What about parents whose genes predispose them to produce disabled offspring? They might have to pay more.

Of course, there will always be those who cannot or do not, for one reason or another, take such precautions. There is still a huge reservoir of charitable impulses and institutions in this country that could offer assistance. And these civil society organizations would be far more robust in a freer health care market.

The Enemy of the Good

Are these perfect solutions? By no means. Perfection is not possible, but market solutions compare very favorably to government solutions, especially over longer periods. Obamacare will continue to bring us unaccountable bureaucracies, shortages, rationing, discouraged doctors, and more.

Some imagine that prior to Obamacare, we had a free-market health insurance system, but the system was already severely hobbled by restrictions.

To name a few:

- It was illegal to offer policies across state lines, which suppressed choices and increased prices, essentially cartelizing health insurance by state.
- Employers were (and still are) given a tax break for providing health insurance (but not auto insurance) to their employees, reducing the incentive for covered employees to economize on health care while driving up prices for individual buyers. People stayed locked in jobs out of fear of losing health policies.
- State regulators forbade policies that excluded certain coverage items, even if policyholders were amenable to such plans.
- Many states made it illegal to price discriminate based on health status.
- The law forbade associated health plans, which would allow organizations like churches or civic groups to pool risk and offer alternatives.
- Medicaid and Medicare made up half of the health care system.

Of course, Obamacare fixed none of these problems.

Many voices are calling for the repeal of Obamacare, but few of those voices are offering the only solution that will work in the long term: complete separation of state and health care. That means no insurance regulation, no medical licensing, and ultimately, the abolition of Medicare and Medicaid, which threaten to wash future federal budgets in a sea of red ink.

Meanwhile, anything resembling real health insurance is illegal. And if you tried to offer it, they might throw you in jail.

Ten Principles of Health Care Reform

- Government should not be determining what is or must be insured. That should be up to the consumers to decide.

- Government should not interfere in contractual relationships between providers and purchasers of insurance, whether individuals or businesses.
- Prices for medical services need to be completely decontrolled, and the convoluted market-rigging by a conspiracy of providers, insurers, and government welfare bureaucracies must be ended.
- Government should not mandate coverage by employers or privilege employer-provided coverage over individually purchased coverage. Third-party payment should be an option.
- Government should not mandate that insurers accept all comers at the same price; that system makes a mockery of the whole idea of insurance itself.
- Discrimination for “pre-existing conditions” should not be a criminal act but rather a rational consideration for determining premiums.
- Government should not restrict who gets to try their hand at providing insurance; entry and exit need to be competitive too.
- Government should never force anyone to pay for a service that he or she does not want. You say coverage is a human right? It’s a human right for a person to refuse coverage.
- If you want to get serious about fixing the system, the byzantine pharmaceutical system has to go. Again, let the consumers decide, and, while we are at it, there should be complete free trade in medicine.
- The 100-year old medical credential monopoly that has so severely restricted entry into the profession should be dismantled. The market is fully capable of assuring quality, and remember too that there is not one definition of quality.

FEE's mission is to inspire, educate, and connect future leaders with the economic, ethical, and legal principles of a free society.

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